

Message Text

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SUBJ: FY 75 LABOR BUDGET: FURTHER DISCUSSION AND ANALYSIS

REF: CANBERRA 6158

1. SUMMARY. THIS IS EXPANSION ON DESCRIPTION AND ANALYSIS OF BUDGET CONTAINED IN REFTEL. WE CONCLUDE THAT LABOR GOVERNMENT, IN ITS ATTEMPT TO ELICIT WAGE RESTRAINT WITH INCOME REDISTRIBUTION AND OTHER MEASURES IN FAVOR OF WAGE EARNERS, IS EMBARKED ON A POLICY WHICH IS LIKELY TO FAIL. END SUMMARY.

2. FY 75 BUDGET PRESENTED BY TREASURER CREAN SEPTEMBER 17 CALLS FOR ESTIMATED EXPENDITURES OF \$A16,274 MILLION, A 32.5 PCT. RISE OVER FY 74 ACTUAL, AND ESTIMATED RECEIPTS OF \$A15,704 MILLION, UP
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30.8 PCT., FOR AN OVERALL DEFICIT OF \$A570 MILLION, ABOUT TWICE

LAST YEAR'S \$A293 MILLION. HOWEVER, ON PURELY DOMESTIC BASIS (AFTER ESTIMATED EXPENDITURES ABROAD ARE DEDUCTED), BUDGET IS ACTUALLY \$A23 MILLION IN SURPLUS.

3. ON EXPENDITURES SIDE LARGEST SHARE GOES TO SOCIAL SECURITY AND WELFARE PROGRAM (21 PCT.); FOLLOWED BY ECONOMIC SERVICES (TRANSPORT, COMMUNICATION, INDUSTRY ASSISTANCE, ETC.) WITH 12 PCT.; EDUCATION, 9 PCT.; DEFENSE, 9 PCT.; HEALTH, 7 PCT.; PUBLIC SERVICES (LEGISLATURE, PUBLIC SAFETY, FOREIGN AFFAIRS, ETC.), 7 PCT.; HOUSING 2 PCT.; URBAN AND REGIONAL DEVELOPMENT, 2 PCT.; AND CULTURE AND RECREATION, 1 PCT. BALANCE (27 PCT) NOT ALLOCATED BY PROGRAM IS MAINLY PAYMENTS TO STATE AND LOCAL GOVERNMENTS. IN RELATIVE TERMS PRINCIPAL GAINER IS EDUCATION WHICH INCREASED ITS SHARE 2.4 PCT. RELATIVE SHARE OF DEFENSE DECLINED 1.6 PCT.

4. MOST NOTABLE FEATURE ON RECEIPTS SIDE IS MASSIVE (45 PCT.) INCREASE IN ESTIMATED INCOME TAX COLLECTIONS. THESE EXPECTED TO MAKE UP 50.7 PCT. OF TOTAL RECEIPTS IN FY 75, COMPARED TO 45.7 PCT. IN FY 74. THE PROPORTION OF ALL OTHER PRINCIPAL TAX REVENUE SOURCES IN TOTAL ESTIMATED RECEIPTS DECLINED, INCLUDING THAT OF COMPANY (CORPORATE INCOME) TAX.

5. IN SPEECH PRESENTING BUDGET TO PARLIAMENT TREASURER CREAN DESCRIBED KEYNOTE OF DOCUMENT AS SOCIAL PROGRESS, AND GOVERNMENT'S OVERRIDING OBJECTIVE TO PROCEED WITH INITIATIVES IN EDUCATION, HEALTH, SOCIAL WELFARE AND URBAN IMPROVEMENT. WHILE HE DESCRIBED FIGHT AGAINST INFLATION AS CRUCIAL, HE NEVERTHELESS SAID IT COULD NOT BE MADE "SOLE OBJECTIVE OF GOVERNMENT POLICY." GOVERNMENT WOULD "ATTACK COST PRICE SPIRAL DIRECTLY" IN DISCUSSIONS WITH STATE GOVERNMENTS, UNIONS AND EMPLOYERS, DEPENDING ON "WIDESPREAD AND UNUSUAL COOPERATION." HE ASSERTED THAT "SUBSTANTIAL REDISTRIBUTION OF INCOMES" WOULD RESULT FROM BUDGET MEASURES IN FAVOR OF WAGE EARNERS AND LOW AND SINGLE INCOME FAMILIES.

6. IN PARLIAMENTARY DEBATE ON DAY FOLLOWING BUDGET PRESENTATION PM WHITLAM VIGOROUSLY DEFENDED BUDGET, HE SAID IT EMBODIED FOUR PRINCIPLES: (A) NO RESORT TO "MASS UNEMPLOYMENT"; (B) PROTECTION OF WEAKER SECTIONS OF COMMUNITY; (C) MOST HELP TO THOSE IN NEED; AND (D) WHERE RESTRAINT REQUIRED, IT WOULD BE SOUGHT FROM STRONGEST AND MOST ABLE TO SHARE LOAD.

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7. FOREGOING OBJECTIVES ARE TO BE ACHIEVED THROUGH SERIES OF MEASURES TO SHIFT TAX BURDEN FROM LOWER INCOME WAGE EARNERS AND TO INCREASE GOVERNMENT EXPENDITURES ON SERVICES TO NEEDIEST. IN TAX REDUCTION AREA THESE INCLUDE RESTRUCTURING RATE SCALE AND DEPENDENT'S ALLOWANCES IN FAVOR OF LOW INCOME FAMILIES, TAX DEDUCTABILITY OF HOME MORTGAGE PAYMENTS, AND ABOLITION OF TV AND RADIO SET LICENSE FEES. INCREASED COLLECTIONS WILL COME, PRESUMABLY FROM HIGHER IN-

COMES, FROM IMPOSITION OF A CAPITAL GAINS TAX, REDUCED EDUCATION EXPENSE ALLOWANCES, TAXATION OF CERTAIN FRINGE BENEFITS, A 10 PCT. SURCHARGE ON TAX ATTRIBUTABLE TO PROPERTY AND OTHER "UNEARNED" INCOME, AMENDED MINING COMPANY TAXES, REDUCED DEDUCTIONS BY LIFE INSURANCE COMPANIES, INCREASED TAX RATE ON PRIVATE COMPANIES, AND INCREASED POSTAL AND OTHER FEES.

8. CREAN TICKED OFF LONG LIST OF PROGRAMS THAT WOULD BENEFIT FROM ADDITIONAL EXPENDITURE. THESE INCLUDED BIG INCREASE (THOUGH FROM A SMALL BASE) IN OUTLAYS FOR URBAN DEVELOPMENT (GROWTH CENTERS, ETC.); 78 PCT. INCREASE IN SPENDING ON EDUCATION; 38 PCT. INCREASE (FROM ALREADY LARGE BASE) ON SOCIAL SECURITY AND WELFARE; 30 PCT. INCREASE ON HEALTH; AND 25 PCT. ON VARIETY OF ECONOMIC SERVICES. LATTER INCLUDES \$A11.8 MILLION FOR STRUCTURAL ASSISTANCE TO INDUSTRIES AND \$A17.8 MILLION FOR NATIONAL EMPLOYMENT AND RETRAINING SYSTEM.

9. COMMENT: TWO ASPECTS OF THE BUDGET ARE ESPECIALLY NOTEWORTHY, ITS IDEOLOGICAL TONE AND ITS POSSIBLE IMPACT ON AUSTRALIA'S SERIOUS INFLATION. THE FIRST, OF COURSE, COMES AS NO SURPRISE WITH THE WHITLAM GOVERNMENT LARGELY FRUSTRATED BY A HOSTILE SENATE SINCE ITS ELECTION IN EFFORTS TO IMPLEMENT PROGRAM OF SOCIAL REFORM AND ECONOMIC RATIONALIZATION. OF MORE IMMEDIATE INTEREST IS BUDGET'S MACROECONOMIC IMPACT. ON A DOMESTIC BASIS IT IS ALMOST IN BALANCE AND THEREFORE, IN CONVENTIONAL FISCAL POLICY TERMS, IS LIKELY TO BE MODERATELY EXPANSIONARY. TO THE EXTENT IT ADDS TO DISPOSABLE INCOMES OF LOWER INCOME WAGE EARNERS (WITH GREATER PROPENSITIES TO CONSUME) IT IS ALSO EXPANSIONARY. ITS EFFECT ON SAVING AND INVESTMENT,

HOWEVER, IS LIKELY TO BE AT LEAST SLIGHTLY CONTRACTIONARY, IF ONLY BECAUSE OF ITS IDEOLOGICAL RING. AND IT REPRESENTS A CONTINUED REFUSAL BY THE LABOR GOVERNMENT TO USE FISCAL POLICY AS AN ANTI-INFLATIONARY INSTRUMENT. MONETARY POLICY THUS WILL CONTINUE TO BEAR THE MAIN BURDEN.

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10. BUT THE BASIS ON WHICH IT WILL STAND OR FALL AS POLICY IS THE EXTENT TO WHICH IT DOES IN FACT "PERSUADE" WAGE EARNERS, BY TAX RATE REDUCTIONS AND OTHER INDUCEMENTS AT THE LOWER INCOME BRACKETS, TO RESTRAIN FUTURE WAGE CLAIMS AND THEREBY MODERATE THE WAGE-PRICE-WAGE SPIRAL. IT IS ON THIS POINT THAT WE ARE MOST SKEPTICAL. THE AVERAGE TAXABLE ANNUAL WAGE INCOME AT THE END OF FY 74 WAS ABOUT \$A6600, \$A1,478 OF WHICH WAS TAKEN IN TAXES, FOR AN AFTER-TAX INCOME OF ABOUT \$A5,100. THE TREASURY ASSUMES FY 75 WAGE INCREASES AVERAGING 22.5 PCT., WHICH WOULD BRING THE AVERAGE EARNER'S BEFORE-TAX INCOME A YEAR LATER UP TO \$A8,000. UNDER THE PROPOSED NEW TAX RATES HE WOULD OWE \$A1,960 OF THIS IN TAXES, FOR AN AFTER-TAX INCOME OF A LITTLE MORE THAN \$A6,000. THE HYPOTHETICAL AVERAGE WAGE EARNER THUS WILL HAVE ENJOYED AN AFTER-TAX INCREASE OF \$A900 OR ABOUT 18 PCT. DURING FY 75 UNDER THE NEW RATES. IF INFLATION RATE

IS HELD TO 18 PCT. OR LOWER DURING THE PERIOD, AVERAGE WAGE-EARNER WILL BE NO WORSE OFF IN REAL TERMS AND MAY EVEN ENJOY SLIGHT IMPROVEMENT. BUT IF INFLATION EXCEEDS 18 PCT., AS IT IS WIDELY EXPECTED TO, WAGE EARNER WILL SUFFER LOSS IN REAL TERMS. IT IS IN EFFORT TO KEEP AHEAD OF INFLATION RATE THAT UNIONS RECENTLY HAVE PRESSED FOR SETTLEMENTS IN 20-30 PCT. RANGE. IF UNION LEADERSHIP IS NOT CONVINCED BUDGET WILL PERMIT AT LEAST MAINTENANCE PRESENT LIVING STANDARDS "WIDESPREAD AND UNUSUAL COOPERATION" GOVERNMENT APPARENTLY RELYING ON IS NOT LIKELY TO BE FORTHCOMING. WE BELIEVE THERE IS HIGH RISK THAT AUSTRALIAN BUDGET ATTEMPT TO WIN A "SOCIAL CONTRACT" WILL FAIL.

11. AS TO FOREIGN TRADE THERE IS RELATIVELY LITTLE IN BUDGET OF DIRECT INTEREST. STRUCTURAL ASSISTANCE AGENCY AND NATIONAL EMPLOYMENT AND TRAINING SYSTEM, REFERRED TO IN PARA 8, ARE LIKELY TO BE USED MAINLY TO HELP ABSORB EFFECTS OF INCREASED IMPORT COMPETITION IN LAST TWO YEARS. PROSPECTS FOR IMPORTS SEEM LITTLE AFFECTED BY BUDGET ITSELF. AS PREVIOUSLY NOTED GOVERNMENT WILL NEED TO RELY ON MONETARY MEASURES IN ITS STABILIZATION POLICIES. WHILE THIS SHOULD INCREASE GOA'S INCENTIVES TO AVOID AUSTRALIAN DOLLAR DEVALUATION, ACCELERATING INFLATION WILL CONTINUE TO REDUCE FOREIGN EXCHANGE RESERVES.
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